

**Testimony on Continued Oversight of the SEC's Offices and Divisions**  
**Before The U.S. House of Representatives Committee on Financial Services**  
**Subcommittee on Capital Markets and Government Sponsored Enterprises**

**Washington, D.C.**  
**April 21, 2016**

Chairman Garrett, Ranking Member Maloney, and Members of the Subcommittee:

Thank you for your invitation to testify on behalf of the U.S. Securities and Exchange Commission (SEC or Commission) about the responsibilities and recent activities of the Division of Economic and Risk Analysis (DERA), the Office of Compliance Inspections and Examinations (OCIE), the Office of Credit Ratings (OCR), and the Office of the Whistleblower (OWB).

In recent years, the SEC has made substantial progress in strengthening its operations and programs. The agency has proposed or adopted nearly all of the mandatory rulemakings required by the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) and the Jumpstart Our Business Startups Act (JOBS Act), in addition to advancing other key rules in mission critical areas that protect investors and our markets. In addition to implementing congressionally mandated rules, the SEC has also advanced other important policy objectives, including rules to enhance oversight of high-frequency traders and the agency's supervision of investment advisers and mutual funds, including reforms to money market mutual funds; as well as adopting requirements for comprehensive new controls at critical market participants to strengthen key technological systems.

Beyond the rulemakings, the SEC has intensified its review of equity and fixed income market structure issues, undertaken a disclosure effectiveness initiative seeking ways to improve the public company disclosure regime for investors and companies, and continued to act aggressively to hold securities law violators accountable. Broad, systemic enhancements in the SEC's National Examination Program (NEP) – including increased recruitment of industry experts, the augmentation of data analytics capacities, and enhanced training programs – have led to a more effective, efficient program. The agency also is increasingly harnessing technology to better identify risks, uncover frauds, sift through large volumes of data, inform policymaking, and streamline operations, while at the same time improving internal collaboration and recruiting more staff with specialized expertise and experience. While these and other critical improvements have been made, challenges remain in the Commission's efforts to address the growing size and complexities of the securities markets and fulfill the SEC's broad mandates and responsibilities. Our testimony will discuss the role each of our divisions and offices play in fulfilling the important mission of the Commission, developments in our respective areas, and some of our recent work.

To continue and expand on our efforts, as set forth in the SEC's FY 2017 budget request, the SEC is requesting \$1.781 billion in support of 5,196 positions and 4,870 full time equivalents (FTE).<sup>1</sup> This requested budget level is essential to support the agency's mission to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation. Specifically, as described in more detail below and consistent with the planning reflected in our recent requests, the budget for FY 2017 seeks to:

- Increase examination coverage of investment advisers and other key entities who interact with retail and institutional investors;
- Further leverage cutting-edge technology to permit the SEC to better keep pace with the entities, markets, and products we regulate;
- Protect investors by enhancing our enforcement program's investigative capabilities and strengthen our ability to litigate against wrongdoers;
- Further bolster the SEC's economic and risk analysis functions; and
- Hire market and other experts to enable the SEC to more expertly and efficiently discharge its current rulemaking and oversight responsibilities.

As you are aware, the SEC's funding is deficit-neutral, which means that any amount appropriated to the agency will be offset by modest transaction fees (approximately \$.02 per \$1,000) and therefore will not impact the deficit or the funding available for other agencies. Our appropriation also does not count against the FY 2016 or FY 2017 caps set in the Bipartisan Budget Act of 2015.

### **DIVISION OF ECONOMIC AND RISK ANALYSIS**

Director and Chief Economist, Mark J. Flannery

The Division of Economic and Risk Analysis supports the Commission's mission through data-driven, high-quality economic analyses. Over the past several years, DERA has grown from approximately 96 employees in 2013 to a projected workforce of 175 by the end of 2016. By that time, DERA anticipates employing 88 Ph.D.s — mostly in economics or finance, but also accountants and two physicists. This set of social scientists is supported by 22 research associates. DERA staff also includes a diverse team of other technical experts and professional staff. The Division's rapid growth and resultant depth of expertise has allowed DERA to expand its support across an ever-increasing range of Commission activities.

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<sup>1</sup> A copy of the SEC's FY 2017 Congressional Budget Justification is available at <http://www.sec.gov/about/reports/secfy17congbudjust.shtml>

## **Rulemaking and Policy Support**

DERA's most well-known function is to provide economic analyses in support of Commission rulemaking and other priority initiatives. DERA economists examine the need for regulatory action, analyze the potential economic effects of proposed and final rules, and evaluate public comments. DERA provides theoretical and data-driven economic analyses of potential new policies and changes to existing policies, working closely with staff from other Commission divisions and offices from the earliest stages of policy development through the finalization of a particular rule. DERA staff also provides analysis, where appropriate, to support the Commission's consideration of self-regulatory organization (SRO), Municipal Securities Rulemaking Board (MSRB), and Public Company Accounting Oversight Board (PCAOB) rules.

In the course of assisting other divisions and offices, staff routinely prepares white papers and other documents that present novel economic analyses of specific policy issues or rulemakings. For example, last year DERA staff published two white papers in conjunction with two of the Division of Investment Management's recent rulemakings — one related to liquidity requirements for open-end mutual funds, and another about funds' derivatives usage. Staff also produced a white paper on voluntary clearing activity in the single-name credit default swap market and a white paper analyzing the market for unregistered securities offerings.

## **Risk Assessment**

DERA also provides financial and risk modeling expertise to other divisions and offices in support of their supervisory, surveillance, and investigative programs related to corporate issuers, broker-dealers, investment companies, and exchanges and trading platforms. Our data analysis helps SEC staff with examination prioritization and scoping, including providing guidance on which entities to examine, and what to look for during the examinations.

DERA recently developed a "Broker-Dealer Risk Assessment" tool in close collaboration with OCIE staff that analyzes how a firm's behavior compares to its peers to identify anomalous behavior that might indicate risks in a broker-dealer's operations, financing, workforce, or structure. The tool also provides predictors of potential misconduct based on risk factors developed using OCIE's historical exam findings. These results help OCIE to prioritize inspections, as well as to focus examiners' attention during an inspection to increase the likelihood of detecting misconduct.

Another recent project — the Corporate Issuer Risk Assessment tool (CIRA) — helps expert staff to assess corporate issuer risk by identifying financial reporting irregularities that may indicate financial fraud. Developed in coordination with the Division of Enforcement, CIRA produces over 200 custom metrics that the staff can use in analyzing issuer behavior and in identifying companies that may warrant further inquiry.

## **Litigation Economics**

DERA staff also support the Division of Enforcement by applying economic theory and statistical methods to answer key questions that arise during investigations, settlement

negotiations, and litigation. In fiscal year 2015, DERA staff provided expert assistance in over 120 new enforcement matters, including accounting fraud, insider trading, and market manipulation cases. DERA staff assists Enforcement staff in identifying securities law violations, quantifying the harm to investors, and calculating ill-gotten gains. DERA staff also evaluate economic-based claims of the defendant — for example, that a penalty would cause a company undue harm. For cases that go to trial, DERA staff work with Enforcement’s Trial Unit to help prepare the Commission’s outside experts and to challenge the work of opposing experts. In certain cases, DERA staff have testified on behalf of the Commission.

## **Data Oversight**

Along with performing complex data analytics, DERA acts as a central hub for the intake, processing, and use of data within the Commission. DERA’s data oversight activities fall into two distinct, but related, categories.

First, DERA works closely with other SEC divisions and offices to design data structuring approaches for required disclosures, and supports the SEC’s data collections and data usage by designing taxonomies, validation rules, data quality assessments, and data dissemination tools to facilitate high-quality data analyses. DERA also works with investors, regulated entities, and the public to support the submission and use of structured data.

Second, DERA is responsible for the day-to-day management of many Commission databases. DERA staff routinely generates summary information and statistics about key aspects of the financial markets, and provide Commission staff with direct access to the underlying data. DERA also develops and refines financial market datasets gathered from sources both internal and external to the Commission.

## **Research**

DERA encourages its staff to be active participants in the academic community, particularly as it investigates and debates topics relevant to the SEC’s mission. Staff regularly have their research papers published in refereed publications that cover finance, economics, and accounting, and staff papers are posted on the DERA webpage of the SEC website to ensure the public can access current research on the financial markets.

## **OFFICE OF COMPLIANCE INSPECTIONS AND EXAMINATIONS**

Director, Marc Wyatt

OCIE, through its National Examination Program, protects investors, ensures market integrity, and supports responsible capital formation through risk-focused strategies that: (1) improve compliance; (2) prevent fraud; (3) monitor risk; and (4) inform policy. The results of OCIE’s examinations are used by the Commission to inform rule-making initiatives, identify and monitor risks, improve industry practices, and identify misconduct.

With a staff of over 1,000 employees, OCIE has examination responsibility for registered entities consisting of more than 12,000 investment advisers, 11,000 mutual funds and exchange-

traded funds, over 4,000 broker-dealers, more than 400 transfer agents and more than 650 registered municipal advisors. OCIE also has oversight responsibility for 18 national securities exchanges, the Financial Industry Regulatory Authority, the Municipal Securities Rulemaking Board, the Securities Investor Protection Corporation (SIPC), six active registered clearing agencies, and the PCAOB. Recent legislative changes by the Dodd-Frank Act and the JOBS Act have expanded OCIE's responsibilities to include examinations of, among others, security-based swap dealers, security-based swap data repositories, major security-based swap participants, securities-based swap execution facilities and crowdfunding portals. Compounding the challenges in the sheer number of registrants is the continued growth in the financial markets and complexity of its participants. For example, over the past fifteen years, assets under management of SEC-registered advisers grew by approximately 210 percent to approximately \$66.8 trillion, and assets under management of mutual funds grew by almost 125 percent to over \$15 trillion today. In order to maximize the use of our limited staff, OCIE is in the formative stages of reallocating examiners across its program to increase coverage of investment advisers.

In fiscal year 2015, examiners in 11 regional offices and headquarters conducted nearly 2,000 examinations, including: 484 examinations of broker-dealers; 1,221 examinations of investment advisers; 137 examinations of investment company complexes; 53 examinations of transfer agents; 6 examinations of clearing agencies; and 50 examinations of municipal advisors. The staff also conducted 21 SRO program examinations and 20 Technology Controls Program examinations, which are inspections of the regulatory operations and automated trading and clearing processes of markets and clearing organizations. Approximately 77 percent of all fiscal year 2015 examinations identified deficiencies and approximately 11 percent resulted in referrals to the Division of Enforcement.

To meet the challenges posed by a registrant population that far exceeds OCIE resources, OCIE has adopted a risk-based approach to examinations, utilized data analytics, and promoted compliance through transparency.

### **Risk-Based Approach**

OCIE has adopted a risk-based examination approach with respect to the firms selected for examination, the areas of the firm examined, and the issues covered. OCIE's Office of Risk Assessment and Surveillance (RAS) aggregates and analyzes data from SEC filings from registrants and individuals to identify activity that may warrant examination. In fiscal year 2015, RAS significantly expanded its data analysis and monitoring efforts to incorporate data from sources internal and external to the Commission, including, for example, data collected by or filed with other regulators, SROs, and exchanges, as well as information that registrants provide to data aggregators regarding, for example, their business activities and marketing-related efforts. This expanded data collection and analysis enhances OCIE's ability to identify operational red flags throughout entire industries – such as firms with aberrant swings in reported assets under management, changes in key individuals, business activities, and affiliates, migration of bad actor industry participants and other possible indicia of heightened risk – and enables examiners to develop a better understanding of firms prior to launching an examination.

## **Data-Driven**

Over the past five years, OCIE has recruited experts to enhance OCIE's technology and its use of data analytics to improve its risk-based examination approach. For example, last fiscal year, OCIE's Quantitative Analytics Unit (QAU) improved the National Exam Analytics Tool, which enables examiners to access and systematically analyze years' worth of a registrant's trading data much faster than ever before. QAU has also been developing technologies to help examiners detect suspicious activity in areas such as money laundering and high frequency trading that will further expand and enhance OCIE's capabilities to fight and deter fraud.

OCIE's Risk Analysis Examination (RAE) Team also uses technology to conduct examinations of some of the nation's largest broker-dealers. By analyzing transactions cleared by firms over several years, RAE has identified possible problematic behavior across multiple firms, including unsuitable recommendations, misrepresentations, inadequate supervision, churning, reverse churning, and load waivers.

## **Enhanced Transparency**

OCIE improves industry compliance with the Federal securities laws and promotes better industry risk management practices through examinations and greater transparency. OCIE engages in extensive communication and outreach initiatives with the industry and other regulators. By communicating with registrants through outreach and published material, OCIE provides registrants with tools to self-assess and remediate any non-compliant behavior on their own. For example, each year, OCIE publishes its annual public statement of examination priorities to inform investors and registrants about areas that the staff believes present heightened risk and to support the SEC's mission.<sup>2</sup>

In addition, OCIE conducted 129 outreach and educational program events in fiscal year 2015, including Compliance Outreach seminars, targeted sessions with never-before-examined advisers, and other outreach initiatives with registrants, regulators, and industry groups. As part of this effort, OCIE also issued six Risk Alerts (among other significant published materials) on such topics as investment advisers and funds that outsource their chief compliance officer function, broker-dealer controls regarding retail sales of structured securities products, and never-before-examined registered investment companies.

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<sup>2</sup> See <https://www.sec.gov/about/offices/ocie/national-examination-program-priorities-2016.pdf>.

## Select Priority Initiatives

Currently, OCIE is pursuing several key initiatives that are critical to the protection of investors.

### *ReTIRE Initiative*

In June 2015, OCIE launched a multi-year examination initiative (ReTIRE), focusing on SEC-registered investment advisers and broker-dealers and the services they offer to investors with retirement accounts.<sup>3</sup> OCIE is focusing on retirement-based savings because retail investors are faced with a complex and evolving set of factors when making critical investment decisions. Some of these factors include the broad and changing array of investments available, the variety of services offered, the changing market environment, and commissions and sales charges associated with these investments. OCIE has and will continue to focus its examinations on certain higher-risk areas of registrants' sales, investment, and oversight processes, with particular emphasis on select areas where retail investors saving for retirement may be harmed, including: the reasonable basis for recommendations; conflicts of interest; supervision and compliance controls; and marketing and disclosure. As of March 10, 2016, OCIE had initiated approximately 200 examinations pursuant to this initiative, which will continue to be a priority in 2016.

### *Cybersecurity*

In the last two years, OCIE has conducted examinations to identify cybersecurity risks and assess cybersecurity preparedness among broker-dealers and investment advisers.<sup>4</sup> These examinations focus on: governance and supervision of information technology systems; operational capability; information security; preparedness for cyber-attacks; access rights and controls; data loss prevention; vendor management; training; and incident response. OCIE made public a summary of its observations and findings. Notable among these was the observation that the vast majority of examined firms conduct periodic risk assessments, on a firm-wide basis, to identify cybersecurity threats, vulnerabilities, and potential business consequences, but fewer firms conduct a similar analysis of vendors.<sup>5</sup> In 2016, OCIE is continuing this effort, including

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<sup>3</sup> See OCIE Risk Alert, "Retirement-Targeted Industry Reviews and Examinations Initiative," June 22, 2015, <http://www.sec.gov/about/offices/ocie/retirement-targeted-industry-reviews-and-examinations-initiative.pdf>.

<sup>4</sup> See OCIE Risk Alert, "OCIE's 2015 Cybersecurity Examinations Initiative," Sept. 15, 2015, <https://www.sec.gov/ocie/announcement/ocie-2015-cybersecurity-examination-initiative.pdf>; OCIE Risk Alert, "OCIE Cybersecurity Initiative," Apr. 15, 2014, <http://www.sec.gov/ocie/announcement/Cybersecurity-Risk-Alert--Appendix---4.15.14.pdf>.

<sup>5</sup> See OCIE Risk Alert, "Cybersecurity Examination Sweep Summary," Feb. 3, 2015, <https://www.sec.gov/about/offices/ocie/cybersecurity-examination-sweep-summary.pdf>.

testing and assessments of firms' implementation of procedures and controls. As of March 11, 2016, OCIE had initiated over 160 examinations pursuant to this initiative.

### *Liquidity Controls*

Amidst the changes in fixed income markets over the past several years, OCIE is examining advisers to mutual funds, ETFs, and private funds that have exposure to potentially illiquid fixed income securities. OCIE will also examine registered broker-dealers that have become new or expanding liquidity providers in the marketplace. These examinations include a review of various controls in these firms' expanded business areas, such as controls over market risk management, valuation, liquidity management, trading activity, and regulatory capital. As of March 11, 2016, OCIE had initiated 193 such examinations. This priority builds on a 2015 priority related to fixed income investment companies.

## **OFFICE OF CREDIT RATINGS**

Director, Thomas J. Butler

With the enactment of the Credit Rating Agency Reform Act of 2006 (CRA Reform Act), Congress provided the Commission with express authority to implement a registration and oversight program for credit rating agencies that elect to be treated as "nationally recognized statistical rating organizations (NRSROs)." As mandated by the Dodd-Frank Act, the Office of Credit Ratings (OCR or the Office) was established at the Commission in June 2012.<sup>6</sup>

OCR is charged with administering the rules of the Commission with respect to the business practices of NRSROs. OCR monitors the activities and conducts examinations of NRSROs to assess and promote compliance with statutory and Commission requirements. OCR collaborates and coordinates with other Commission offices and divisions as warranted to enhance its ability to serve the public interest and protect users of credit ratings.

Pursuant to the Dodd-Frank Act, OCR staff includes persons with knowledge of and expertise in corporate, municipal and structured debt finance. OCR is currently comprised of approximately 50 staff members located in New York and Washington, D.C. OCR's activities fall within the following areas: Examinations; NRSRO Monitoring and Constituent Monitoring; and Policy and Rulemaking, each of which is briefly described below.

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<sup>6</sup> Prior to the establishment of OCR, examinations of the NRSROs were conducted by the Office of Compliance Inspections and Examinations, and NRSRO monitoring was undertaken by the Division of Trading and Markets.



## Examinations

Examinations of NRSROs for compliance with federal securities laws and Commission rules account for the majority of OCR's activity. The Dodd-Frank Act requires that OCR conduct an examination of each NRSRO at least annually.

The scope of the annual examinations covers eight review areas prescribed by the Dodd-Frank Act. Further, OCR employs a risk-based approach to exam planning, identifying different risks for different NRSROs. This improves the efficiency and the effectiveness of the NRSRO examinations, as resources are prioritized and focused on areas of higher risk. The examinations of the NRSROs may include a quantitative analyst to provide analytical support directly alongside the examination teams. In addition to the annual examinations, OCR conducts sweeps and targeted examinations to: (1) address credit market issues and concerns; and (2) follow up on tips, complaints, and NRSRO self-reported incidents.

In conducting an NRSRO examination, OCR staff reviews, among other things: (1) the implementation of policies and procedures to assess compliance with the rules; (2) selected ratings files in connection with ratings issuances and surveillance activities; (3) internal controls and governance activities; and (4) internal compliance reports. As part of the examination, OCR examiners travel onsite to an NRSRO and conduct interviews of management and staff, including credit rating analysts, as well as members of the NRSRO's board of directors.

To date, the NRSROs have been generally responsive to the Commission staff's findings and recommendations. Many have implemented fundamental changes, such as: increasing surveillance activities; strengthening policies and procedures for managing conflicts of interest; adding compliance staff and restructuring oversight functions within the organization; investing in multi-year technology initiatives; and enhancing disclosure, transparency and governance. The annual examinations that are currently underway include a comprehensive review of NRSROs' compliance with the significant new rules and rule amendments that were adopted by the Commission in August 2014, most of which became effective in June 2015.

As required by the Dodd-Frank Act, OCR prepares an annual public examination report summarizing: (1) the essential findings of the examinations; (2) responses by the NRSROs to any material regulatory deficiencies identified by the Commission; and (3) whether the NRSROs have appropriately addressed previous examination recommendations. In December 2015, OCR published the fifth annual public examination report.<sup>7</sup>

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<sup>7</sup> <http://www.sec.gov/ocr>

One important area complementing OCR's examinations is the potential for referral to the Commission's Division of Enforcement of any of the staff's findings. Past examinations have, in certain instances, led to enforcement referrals.

### **NRSRO Monitoring and Constituent Monitoring**

The NRSRO Monitoring and Constituent Monitoring groups gather, analyze and assess data and identify trends across the industry. This information provides useful input for examination scoping, determining and communicating best practices for NRSROs and guiding the direction for any future rulemakings related to NRSROs. Both groups also work collaboratively with, and serve as a resource to, other divisions and offices throughout the Commission.

NRSRO Monitoring conducts periodic meetings with NRSROs separate from the examination function, and may also meet on an *ad hoc* basis at an NRSRO's request or proactively as necessary to respond to NRSRO or industry developments. The group meets with certain NRSRO boards of directors (including a separate discussion with the independent directors), in addition to the meetings with the directors that the OCR examiners conduct, in an effort to engage the directors in broader policy discussions. NRSRO Monitoring is also responsible for reviewing the annual and periodic registrant updates submitted on Form NRSRO, reviewing the NRSRO Employment Transition Reports for former employees of NRSROs, and receiving tips from NRSROs that are reported pursuant to Section 15E(u) of the Securities Exchange Act.

Constituent Monitoring holds meetings with investors, issuers, arrangers, and industry trade groups. The group conducts *ad hoc* research as warranted by industry or credit market conditions. The group also discusses matters of common interest with other U.S. government agencies. Constituent Monitoring analyzes the differences in types of investors that affect their reliance on credit ratings and their views of NRSROs, the profiles of investor organizations and regulatory issues faced by other industries (*e.g.*, investment banking, commercial banking, and accounting) that are akin to NRSRO issues, and how other industries may have addressed similar issues.

### **Policy and Rulemaking**

The Policy and Rulemaking group is responsible for developing rule recommendations for the Commission's consideration. The group also reviews requests for Commission exemptive relief or staff "no-action" relief from existing rule requirements. The group is instrumental in formulating staff guidance and other interpretive positions for OCR. The group receives feedback from the NRSRO examinations and from OCR's monitoring activities to help inform its policy recommendations. The Policy and Rulemaking group also reviews initial applications for NRSRO registration and applications from existing NRSROs for registration in additional ratings classes.

Pursuant to the CRA Reform Act, the Commission adopted rules establishing a regulatory oversight program for NRSROs and thereafter adopted amendments to several of those rules. The Commission's rules established a registration program for NRSROs and imposed disclosure, recordkeeping and reporting requirements. The Commission has broad authority to: (1) examine all books and records of an NRSRO; and (2) impose sanctions for violating statutory provisions and the Commission's rules. However, the Commission is not permitted to regulate the substance of credit ratings or the procedures and methodologies used to determine credit ratings.

As required by the Dodd-Frank Act, the Commission adopted a comprehensive set of new rules and rule amendments to strengthen the integrity and improve the transparency of credit ratings.<sup>8</sup> The rules address, among other things: reporting on internal controls; conflicts of interest with respect to sales and marketing practices, including the requirement to separate sales and marketing activities from analytics; disclosure of credit rating performance statistics; procedures to protect the integrity and transparency of rating methodologies, including the requirement for the NRSRO's board of directors to approve a methodology before it is used; disclosures to promote the transparency of credit ratings; and standards for training, experience and competence of credit analysts. The requirements provide for an annual certification by the CEO as to the effectiveness of internal controls and additional certifications to accompany credit ratings attesting that no part of the credit rating was influenced by any other business activities.

The Policy and Rulemaking group in OCR is responsible for conducting studies and drafting reports, including those required under the CRA Reform Act and the Dodd-Frank Act. In December 2015, OCR published the eighth Annual Report on NRSROs, as required under the CRA Reform Act.<sup>9</sup> The report provides a snapshot of the industry, including staff views on competition, transparency and conflicts of interest.

### **OFFICE OF THE WHISTLEBLOWER**

Chief, Sean McKessy

Pursuant to the Dodd-Frank Act, the Commission established the Office of the Whistleblower (OWB), a separate office within the Division of Enforcement, to administer the whistleblower program. OWB is currently comprised of 11 staff attorneys, 5 legal assistants, and an administrative assistant.

The whistleblower program was designed to incentivize individuals to provide the Commission with specific, credible and timely information about possible federal securities law

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<sup>8</sup> <http://www.sec.gov/rules/final/2014/34-72936.pdf>.

<sup>9</sup> <http://www.sec.gov/ocr>

violations, and thereby enhance the Commission's ability to act swiftly to protect investors from harm and bring violators to justice. Under the program, individuals who voluntarily provide the Commission with original information that leads to a successful enforcement action resulting in monetary sanctions over \$1 million, may be eligible to receive an award equal to 10-30% of the monies collected by the Commission or in a related action.

Since the whistleblower program went into effect in August 2011, the Commission has awarded more than \$57 million to 27 whistleblowers. In Fiscal Year 2015 alone, more than \$37 million was paid to reward whistleblowers for their provision of original information that led to a successful Commission enforcement action with monetary sanctions totaling over \$1 million. All payments are made out of an investor protection fund established by Congress that is financed entirely through monetary sanctions paid to the Commission by securities law violators.

Because of the information and assistance provided by the 27 whistleblowers who received awards under the program, the Commission was able to bring successful enforcement actions where over \$400 million was ordered in sanctions, including over \$325 million in disgorgement for harmed investors. Over \$350 million has been collected in connection with these Commission actions as well as successful related actions.

One of the primary activities of OWB is to evaluate whistleblower award claims and to make recommendations as to whether claimants satisfy the eligibility requirements for receiving an award. The Claims Review Staff, designated by the Director of Enforcement, considers OWB's recommendations in accordance with the criteria set forth in the Dodd-Frank Act and the Commission's final rules, and issues a Preliminary Determination. All Preliminary Determinations involving an award, as well as contested denials, are forwarded to the Commission for consideration, which then issues a Final Order. By the end of Fiscal Year 2015, the Commission and Claims Review Staff had issued Final Orders and Preliminary Determinations with respect to over 390 claims for whistleblower awards.

The number of whistleblower tips received by the Commission has increased each year of the program's operation. In Fiscal Year 2015, the Commission received nearly 4,000 whistleblower tips, representing a 30% increase over the number of tips received in Fiscal Year 2012, the first year for which OWB had full-year data. Since August 2011, the Commission has received more than 14,000 whistleblower tips. OWB has received whistleblower tips from individuals in every state in the country, as well as the District of Columbia, and from individuals in 95 foreign countries.

OWB also continues to receive a significant number of award claims. In Fiscal Year 2015 alone, OWB received more than 120 whistleblower award claims. OWB believes the uptick in whistleblower award claims and whistleblower tips is likely attributable to the increased public awareness of the Commission's whistleblower program and in response to the tens of millions of dollars that have been paid to whistleblowers under the program.

In addition to managing the awards program, OWB is actively involved with the investigative staff in helping to ensure that employees feel secure in reporting wrongdoing to the

Commission, without fear of reprisal from their employers. In June 2014, the Commission brought its first enforcement action under the anti-retaliation provisions of the Dodd-Frank Act.<sup>10</sup> The Commission's action sent a strong message to employers that retaliation against whistleblowers in any form is unacceptable. The Commission also has filed several *amicus curiae* briefs in private cases pending in the federal courts to address the scope of the anti-retaliation employment protections established by the Dodd-Frank Act. The Commission argued that the employment protections should be understood to protect individuals at publicly-traded companies from employment retaliation who internally report potential securities law violations, regardless of whether they have separately reported the information to the Commission.

In April 2015, the Commission brought its first enforcement action against a company for including language in confidentiality agreements that impeded whistleblowers from reporting to the Commission.<sup>11</sup> Exchange Act Rule 21F-17(a) provides that no person may take any action to impede an individual from reporting information about wrongdoing to the Commission. This includes, for example, by enforcing, or threatening to enforce, a confidentiality agreement with respect to such reporting. Protecting whistleblowers' rights to report possible securities law violations to the Commission, and protecting whistleblowers from retaliation, continues to be a top priority for OWB.

By protecting the confidentiality of individuals who report to the Commission pursuant to the whistleblower program, taking action against employers who retaliate against or interfere with their employees' ability to report wrongdoing to the agency, and awarding whistleblowers whose information leads to successful enforcement actions, OWB expects that the Commission will continue to receive high-quality tips that can be leveraged to detect and halt fraud earlier and more effectively. OWB anticipates that the whistleblower program will continue to be a game changer in the enforcement of the federal securities laws and the protection of investors and the marketplace.

## **Conclusion**

In many ways the division and offices we supervise represent the evolving approach to securities regulation and oversight compelled by the recent financial crisis and guided by Congress. The Commission continues to make progress in adapting its operations to rapidly changing market conditions with the knowledge that our efforts will be ongoing. We look forward to continuing to work with Congress in this endeavor and we are happy to answer any questions you may have.

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<sup>10</sup> *In the Matter of Paradigm Capital Mgmt., Inc.*, File No. 3-15930, Rel. No. 72393 (June 16, 2014).

<sup>11</sup> *In the Matter of KBR, Inc.*, File No. 3-16466, Rel. No. 74619 (Apr. 1, 2015).